

GAO

United States General Accounting Office

Report to the Chairman, Committee on
the Budget, House of Representatives

April 1997

RURAL DEVELOPMENT

Financial Condition of the Rural Utilities Service's Loan Portfolio



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Resources, Community, and
Economic Development Division

B-275588

April 11, 1997

The Honorable John R. Kasich
Chairman, Committee on the Budget
House of Representatives

Dear Mr. Chairman:

To assist in the development of infrastructure in the nation's rural areas, the Rural Utilities Service (RUS) in the U.S. Department of Agriculture (USDA) made or guaranteed about \$10.4 billion in loans during fiscal years 1992 through 1996. Because of the concerns you raised about the financial risks associated with RUS' lending, we examined the (1) financial condition of the electricity, telecommunications, and water and waste disposal loan portfolios and (2) financial characteristics of borrowers having electricity and telecommunications loans.¹ We did not examine the financial characteristics of borrowers with water and waste disposal loans because most are public entities rather than private firms.

Results in Brief

At the end of fiscal year 1996, over \$8 billion of the total \$42.5 billion in outstanding principal on the Rural Utilities Service's electricity, telecommunications, and water and waste disposal loans was owed by borrowers that were experiencing financial problems (i.e., they were delinquent, in bankruptcy, or likely to default on loan repayment in the future). Almost all of this amount was owed by 12 electricity loan borrowers, representing less than 2 percent of the total number of electricity loan borrowers. These 12 borrowers owed almost 25 percent of the outstanding electricity loan portfolio. Of the \$5.2 billion in outstanding principal on the telecommunications loans, none was owed by borrowers experiencing similar financial distress. Of the slightly more than \$5 billion in outstanding principal on water and waste disposal loans, \$43 million was owed by 70 delinquent borrowers that made up less than 1 percent of total borrowers and that owed less than 1 percent of the outstanding portfolio.

Most electricity and telecommunications loan borrowers had favorable financial characteristics at the end of calendar year 1995. For example, year-end reports to the Rural Utilities Service showed that more than 98 percent of the electricity loan borrowers and more than 99 percent of the

¹RUS operates loan programs formerly administered by other USDA agencies. In this report, we refer to these loans and programs as RUS' loans and programs.

telecommunications loan borrowers had positive equity at the end of 1995. About 95 percent, or a total of 1,610 borrowers, had equity of \$1 million or more. Similarly, the year-end reports showed that about 96 percent of the electricity loan borrowers and about 98 percent of the telecommunications loan borrowers made a profit in 1995. About 92 percent, or a total of 1,565 borrowers, made a profit of \$100,000 or more. However, 10 electricity and 3 telecommunications loan borrowers had negative equity at the end of 1995. Nine of these electricity loan borrowers owed about \$6.2 billion as of September 30, 1996; the loans of the 10th borrower were resolved prior to that date when the borrower made a partial payment and the agency wrote off the remaining debt. The three telecommunications loan borrowers owed about \$5.4 million as of September 30, 1996. Also, 38 electricity and 14 telecommunications loan borrowers did not make a profit in 1995; these borrowers owed about \$1.2 billion and about \$103 million, respectively, as of September 30, 1996.

Background

USDA is the federal government's principal provider of loans used to assist the nation's rural areas in developing their utility infrastructure. Through RUS, USDA finances the construction, improvement, and repair of electrical, telecommunications, and water and waste disposal systems. The agency provides credit assistance through direct loans and through repayment guarantees on loans made by other lenders.

Electricity loans are made primarily to electric cooperatives; more than 99 percent of the borrowers with electricity loans are nonprofit cooperatives. Direct loans are made to construct and maintain the distribution facilities that provide electricity to users, and guarantees are provided on loans to finance the construction of electricity generating and transmission facilities. Telecommunications loans—both direct and guaranteed—are made primarily to telephone cooperatives and commercial companies to build and improve telephone and telecommunications facilities and services; about 28 percent of the borrowers with telecommunications loans are nonprofit cooperatives, and about 72 percent are for-profit companies. RUS also administers the Rural Telephone Bank (RTB) loan program, in which direct loans are made to supplement the financing that telephone cooperatives and commercial companies receive from RUS through the telecommunications loan program.² Water and waste disposal loans, either direct or guaranteed, are made to public bodies and nonprofit associations; about 80 percent of the borrowers with water and waste

²RTB is a government-private corporation with federal agency status until it is privatized through the retirement of the stock that the government owns. Privatization began in fiscal year 1996, when RTB purchased \$18 million of the federally owned stock.

disposal loans are public bodies, and about 20 percent are nonprofit associations. Water loans are made to improve the storage, treatment, and distribution of water, and waste disposal loans are made to collect, treat, and dispose of waste, including solid waste and storm drainage. (App. I provides additional details on each of the utility loan programs.)

RUS' Recent Loan Obligations

During fiscal years 1992 through 1996, RUS made or provided USDA guarantees on slightly more than 6,150 utility loans, which totaled about \$10.4 billion. Table 1 shows the level of loans in each of the utility programs.

Table 1: Total Number and Amount of Utility Loans Made or Guaranteed by RUS, Fiscal Years 1992-96

Program	Dollars in millions		
	Total number of loans	Total dollar amount of loans	Average dollar amount of loans
Electricity	880	\$ 4,352.4	\$4.9
Telecommunications ^a	510	2,575.1	5.0
Water and waste disposal	4,764	3,464.3	0.7
Total	6,154	\$10,391.8	\$1.7

^aIncludes Rural Telephone Bank loans.

Sources: USDA, Budget Explanatory Notes for Committee on Appropriations, fiscal years 1994 through 1997; RUS' reports; and as calculated by GAO.

Direct loans accounted for 6,033 of the total loans and for \$8.9 billion of the total loan amount. The other 121 loans had USDA guarantees—83 loans were electricity or telecommunications loans, and 38 were water and waste disposal loans. All electricity and telecommunications loans that received USDA repayment guarantees during this 5-year period were made by the Treasury's Federal Financing Bank (FFB);³ all water and waste disposal loans that received guarantees were made by commercial lenders. (App. I provides detailed information on direct and guaranteed loans in each of the utility loan programs for fiscal years 1992 through 1996.)

RUS' Recent Cost for Operating the Utility Loan Programs

RUS' cost for the utility loan programs totaled about \$1.4 billion in fiscal years 1992 through 1996. This cost consists of two components: federal subsidy costs and administrative costs for salaries and other expenses. The subsidy cost under credit reform (post-fiscal year 1991 credit)

³Loans made by the FFB that have USDA repayment guarantees are treated in RUS' financial statements as direct loans.

includes net present value estimates of (1) the interest costs associated with loans made at rates below the rate at which RUS borrows from the Treasury, (2) default costs, (3) fees, and (4) other costs and revenues.⁴ (App. I presents a more detailed discussion of the principles and requirements of credit reform.) Table 2 shows RUS' reported costs for each of the utility programs.

Table 2: RUS' Total Costs for Utility Loans, Fiscal Years 1992-96

Dollars in millions			
Program	Subsidy costs	Administrative costs ^a	Total costs ^b
Electricity	\$ 446.2	\$105.1	\$ 551.3
Telecommunications ^c	108.3	82.0	190.3
Water and waste disposal	544.7	154.9	699.7
Total^b	\$1,099.2	\$342.1	\$1,441.3

^aRUS' administrative costs apply to the operation of both direct and guaranteed loans. The amounts shown do not include any costs that the FFB or commercial lenders may have incurred.

^bTotals may not add due to rounding.

^cIncludes the costs of Rural Telephone Bank loans.

Sources: Obligation data on subsidy costs obtained from USDA, Budget Explanatory Notes for Committee on Appropriations, fiscal years 1994 through 1997, and the Budget Division of USDA's Rural Development mission area. Administrative costs were obtained from the latter.

About 54 percent of RUS' total subsidy costs on electricity loans involved loans made in fiscal years 1992 and 1993; the remaining 46 percent involved loans made during fiscal years 1994 through 1996. On telecommunications loans, about 69 percent of the total subsidy costs involved loans made in the first 2 fiscal years, and 31 percent involved loans made in the last 3 fiscal years. On the other hand, about 31 percent of the total subsidy costs on water and waste disposal loans involved loans made in fiscal years 1992 and 1993, and 69 percent involved loans made in fiscal years 1994 through 1996.

Almost 99 percent of RUS' total subsidy costs involved direct loans. About 59 percent of the electricity loans were direct loans made at a 5 percent interest rate; these loans accounted for about 42 percent of the total dollar amount of all electricity loans. About 24 percent of the telecommunications loans were direct loans made at a 5 percent interest

⁴The Federal Credit Reform Act of 1990, which was included as Title 13B of the Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508, Nov. 5, 1990) changed the way post-fiscal year 1991 credit programs are reported in the budget by ensuring that their subsidy costs were considered in making resource allocation decisions.

rate; these loans accounted for about 27 percent of the total dollar amount of all telecommunications loans. Also, about 91 percent of the water and waste disposal loans were direct loans made at interest rates that were less than RUS' costs of borrowing from the Treasury; these loans accounted for about 87 percent of the total dollar amount of all water and waste disposal loans. (App. I discusses loans with subsidized interest rates.)

We did not assess the accuracy of RUS' reported subsidy cost estimates or the adequacy of the system used by RUS to derive such estimates under credit reform. (App. I provides detailed information on the reported costs for the direct and guaranteed loans in each of the utility loan programs for fiscal years 1992 through 1996, and further discussion of subsidy costs.)

Financial Condition of Portfolio

The outstanding principal on RUS' direct and guaranteed electricity, telecommunications, and water and waste disposal loans totaled \$42.5 billion at the end of fiscal year 1996.⁵ About \$660 million of the total outstanding principal was owed by borrowers that were delinquent (at least 30 days past due on loan repayment)—about \$618 million by delinquent borrowers with electricity loans and about \$43 million by delinquent borrowers with water and waste disposal loans. The telecommunications loan portfolio had no delinquencies. Much more of the outstanding electricity loan principal is at risk, however, because it is owed by other borrowers that are experiencing financial distress; for example, they are in bankruptcy or, according to RUS officials, are likely to default on loan repayment in the near future. RUS' records show that a total principal of \$7.4 billion was owed by such borrowers at the end of fiscal year 1996. Four borrowers whose loans had previously been restructured (the original loan agreements were altered, including revised repayment schedules and changes in interest rates) and that continue to be in severe financial trouble owe \$5.7 billion; four other borrowers whose loans had not previously been restructured and that are also in serious financial difficulty owe \$1.1 billion; and, one other borrower whose loans had previously been restructured and that informed RUS in early fiscal year 1997 that it was experiencing financial difficulties owes \$0.6 billion. Most of the electricity loans to RUS' problem borrowers were made many years ago—some dating back to the late 1970s.

⁵The information in this section of the report discusses the outstanding principal on the loans made or guaranteed by RUS. We have not adjusted the outstanding loan amounts to reflect the allowance for losses that RUS includes in its financial statements. Also, while borrowers have pledged collateral property as security for the loans, we did not determine the extent to which such property protects the government's investments in the outstanding utility loans.

This relatively high dollar amount of problem loans exists even though RUS had written off some borrowers' debts in recent years. Most of the write-offs have involved electricity loans, but some water and waste disposal loans have also experienced write-offs. Specifically, RUS wrote off almost \$1.05 billion in electricity loans during the 5-year period, fiscal years 1992-96. It also wrote off \$6 million in water and waste disposal loans during this period.

Electricity Loans

According to RUS' reports, about \$8 billion, or almost 25 percent of the \$32.3 billion in outstanding principal on electricity loans as of September 30, 1996, was owed by 12 borrowers that are delinquent or in financial distress. These 12 borrowers made up less than 2 percent of the total number of RUS' electricity loan borrowers.

About \$618 million of principal was owed by three delinquent borrowers. These three borrowers, each of which had been delinquent since the mid-1980s, also owed almost \$400 million in unpaid interest. Table 3 shows the amount of principal owed by all borrowers, and the portion owed by delinquent borrowers, on electricity loans at the end of fiscal year 1996. (App. II provides information on electricity loans at the end of fiscal years 1992 through 1995.)

Table 3: Amount of Outstanding Principal on Electricity Loans Made or Guaranteed by RUS, and Portion Owed by Delinquent Borrowers, as of September 30, 1996

Dollars in millions		
Loan type	Outstanding principal owed by all borrowers	Amount owed by delinquent borrowers
RUS' direct loans	\$11,475.2	\$ 29.6
Guaranteed FFB loans	13,328.6	572.0
Other guaranteed loans	664.7	16.3
Restructured loans ^a	6,841.1	0
Total	\$32,309.6	\$617.9

^aIncludes previously issued (1) direct loans made by RUS, (2) guaranteed loans made by the FFB, (3) guaranteed loans made by commercial lenders on which RUS agreed to be directly liable for repaying the loan, and (4) loans that had been owed by borrowers now assumed by other utilities. The amounts cover the principal and the capitalized interest owed on the loans. The loans in this category are not included in the other direct and guaranteed loan categories.

Source: RUS' reports.

Each of the three delinquent borrowers has filed for bankruptcy. According to RUS officials, two of the borrowers (a distribution borrower and a power supply borrower) have problems that stem from investments

in the same nuclear-generating plant, which resulted in high levels of debt and debt-servicing expenses, coupled with a lack of growth in their customer bases. At the end of fiscal year 1996, the distribution borrower owed \$15.1 million in outstanding principal and \$4 million in unpaid interest on RUS' direct loans. The power supply borrower owed \$41.2 million in principal and \$21.5 million in interest on RUS' direct and guaranteed loans. Both borrowers filed for bankruptcy in April 1996. The third delinquent borrower has a high debt level because it invested in a nuclear-generating plant that was not completed. This power supply borrower, which owed \$561.5 million in principal and \$373.4 million in interest on loans guaranteed by RUS, has been in bankruptcy since 1985.

In addition to delinquent borrowers, the electricity loan program had other problem borrowers at the end of fiscal year 1996. These include four power supply borrowers that previously had their debts restructured and that continued, according to RUS officials, to be in severe financial trouble. According to the RUS officials, these borrowers' problems stem from their investments in nuclear-generating plants that were completed late and over budget or in coal-fired generating plants that were built to satisfy anticipated industrial growth that did not occur. These borrowers' debts had been restructured at least once in the 1980s or the early part of 1990. Two of these borrowers had filed for bankruptcy: One, with \$4.2 billion in outstanding loans, filed in 1994, and the other, with \$531 million in outstanding loans, filed in 1996. The third borrower with \$293 million of debt was negotiating the resolution of its outstanding loans at the time of our review. The fourth borrower, with more than \$700 million in outstanding loan principal and about \$36 million in accrued interest, had agreed in late 1995 to provide a lump-sum payment to settle its electricity debt. (In mid-October 1996, this borrower paid RUS about \$240 million, and RUS forgave slightly more than \$500 million.)

Furthermore, according to RUS officials, four other power supply borrowers, none of which have had their debts restructured, were also in serious financial difficulty at the end of fiscal year 1996. RUS' automated records show that, as of September 30, 1996, these four borrowers owed a total principal of about \$1.1 billion on direct and guaranteed electricity loans.

RUS officials also told us that another power supply borrower, which had had its debts restructured in the mid-1980s, had requested in October 1996 that RUS consider renegotiating its debt because it does not expect to remain financially viable due to increasing competition and a high

debt-service expense. As of September 30, 1996, this borrower owed \$562.3 million of principal on direct and guaranteed loans.

RUS continues to experience problems with its electricity loan portfolio even though it wrote off \$1,047.4 million for three borrowers from fiscal years 1992 through 1996. These three borrowers had had their debts restructured prior to the agreements that resulted in the RUS write-offs; none was delinquent on the terms of the restructured loans when the debt settlement agreements were completed. These three borrowers were a distribution borrower that had \$13.7 million written off in February 1994, a power supply borrower that had \$51.7 million written off in August 1995, and another power supply borrower that had about \$982 million written off in September 1996.

RUS' electricity loan portfolio faces the possibility of additional financial stress due to increasing competition among the providers of electricity. For example, as we previously reported,⁶ competition in the wholesale electricity market is increasing as a result of legislation that was enacted in the early 1990s, such as the Energy Policy Act of 1992 (P.L. 102-486, Oct. 24, 1992). The act encouraged additional wholesale suppliers to enter the electricity market and provided greater access to other utilities' transmission lines.

Telecommunications Loans

According to RUS' reports, the outstanding principal owed on telecommunications loans totaled \$5.2 billion as of September 30, 1996. Of this amount, RUS' direct loans accounted for \$3.4 billion, loans guaranteed by RUS accounted for \$320 million (\$318 million on FFB loans and \$2 million on non-FFB loans), and RTB's direct loans accounted for \$1.5 billion. (App. II provides information on telecommunications loans at the end of fiscal years 1992 through 1995.)

RUS' telecommunications loan program does not display the level of risk that exists in the electricity loan program or, to a lesser extent in the water and waste disposal loan program. Specifically, there were no delinquencies on these loans.⁷ In addition, the RUS telecommunications

⁶Power Marketing Administrations: Cost Recovery, Financing, and Comparison to Nonfederal Utilities (GAO/AIMD-96-145, Sept. 19, 1996) and Federal Electric Power: Operating and Financial Status of DOE's Power Marketing Administrations (GAO/RCED/AIMD-96-9FS, Oct. 13, 1995).

⁷We do not include as delinquent those telecommunications loan borrowers that are shown in RUS' reports as being past due on repayments when the delinquency was due to billing, payment, or administrative errors and when the past due amount was paid shortly after the start of the next fiscal year.

loan portfolio has no loans that have been restructured because of past repayment problems or that had been flagged by the agency's officials as being in serious financial difficulty. Furthermore, RUS did not write off the debt of any telecommunications loan borrowers during fiscal years 1992 through 1996.

However, the industry in which RUS' telecommunications loan borrowers operate is changing. In particular, as we previously reported,⁸ there have been rapid advances in technology and changes in the legislative environment, such as the Telecommunications Act of 1996 (P.L. 104-104, Feb. 8, 1996). These factors could work to either the betterment or the detriment of the borrowers that have telecommunications loans.

Water and Waste Disposal Loans

According to RUS' reports, less than 1 percent of the outstanding principal on water and waste disposal loans was owed by borrowers that were delinquent. Specifically, the outstanding principal on water and waste disposal loans totaled slightly more than \$5 billion as of September 30, 1996; direct loans accounted for all but about \$8 million of this amount. On the direct loans, 70 delinquent borrowers owed \$43.3 million at the end of fiscal year 1996. These 70 borrowers made up less than 1 percent of the total number of water and waste disposal direct loan borrowers. On guaranteed loans, there were no delinquencies. (App. II provides information on water and waste disposal loans at the end of fiscal years 1992 through 1995.)

When borrowers have had problems repaying their water and waste disposal loans on schedule, RUS has changed their repayment schedules. During fiscal years 1992 through 1996, 33 borrowers had their repayment schedules revised; these borrowers owed RUS \$54.1 million at the end of fiscal year 1996. There was no debt forgiveness associated with these payment changes.

RUS has, however, provided debt relief to other problem borrowers. During fiscal years 1992 through 1996, RUS forgave slightly more than \$6 million in settling the accounts of 12 water and waste disposal loan borrowers. These write-offs ranged from slightly less than \$6,000 for a borrower whose debt was resolved through bankruptcy to \$3.1 million for a local development authority following the transfer of its assets and debts to another public body.

⁸Rural Development: Steps Toward Realizing the Potential of Telecommunications Technologies (GAO/RCED-96-155, June 14, 1996) and Telecommunications: Initiatives Taken by Three States to Promote Increased Access and Investment (GAO/RCED-96-68, Mar. 12, 1996).

Financial Characteristics of RUS' Electricity and Telecommunications Borrowers

While the majority of borrowers with electricity or telecommunications loans had generally favorable financial characteristics, some did not. Specifically, RUS has automated records that contain the financial data submitted by about 96 percent of its 1,778 electricity and telecommunications loan borrowers at the end of 1995.⁹ While the overwhelming majority of borrowers had positive equity at the end of 1995, 13 borrowers, or about 1 percent, had negative equity. Also, while most had a profit as a result of 1995 operations, 52 borrowers, or 3 percent, had a loss.¹⁰ Furthermore, 14 of the 52 borrowers that had losses in 1995 also had losses in at least 1 year between 1992 and 1994.

Electricity Loans

RUS' automated files contained financial information for 804 distribution borrowers and 51 power supply borrowers with outstanding electricity loans (direct and/or guaranteed loans) at the end of 1995. On the basis of the measures we used, which included net worth and net income, we found that even though the dollar amount of problem electricity loans was relatively large, most, but not all, electricity loan borrowers had generally favorable financial characteristics. For example, the distribution borrowers had average assets of \$37.4 million, liabilities of \$21.6 million, and a net worth of \$15.8 million. All but five of these borrowers had \$1 million or more of net worth; however, two had a negative net worth. These two borrowers owed about \$32 million on their outstanding electricity loans as of September 30, 1996. In comparison, power supply borrowers had average assets of \$633 million, liabilities of \$622.1 million, and a net worth of \$10.9 million. Of the power suppliers, 42 had \$1 million or more of net worth, but 8 had a negative net worth. Seven of these 8 borrowers owed about \$6.1 billion on their outstanding electricity loans as of September 30, 1996. The electricity loans of the eighth borrower were settled on September 13, 1996, when the borrower made a partial payment and RUS wrote off the remaining debt.

Another financial characteristic of the borrowers with electricity loans is the net income they made in 1995. The distribution borrowers had average operating revenues of \$18.9 million, operating expenses of \$17.2 million, and a net operating income of \$1.7 million. Overall, they had a total profit of \$1 billion, or about \$1.3 million on average. All but 34, or 4.2 percent, of

⁹The information presented in this section of the report on borrowers' financial characteristics is calendar year data taken from RUS' databases. While RUS' files contain financial information on the majority of its borrowers, they did not include financial data for the year ending 1995 for 4 of the 12 electricity loan borrowers that were delinquent or experiencing financial difficulty.

¹⁰RUS refers to the profits made by electricity and telecommunications loan borrowers that are nonprofit cooperatives as "net margins" and to the losses as "deficits in net margins."

these borrowers had a profit in 1995. The 34 borrowers that had a loss owed \$359 million on their outstanding electricity loans as of September 30, 1996. Furthermore, 10 of these 34 borrowers had losses in at least 1 year between 1992 and 1994. In comparison, the power suppliers had average operating revenues of \$190.3 million, operating expenses of \$161.5 million, and a net operating income of \$28.8 million. Overall, the power suppliers had \$234 million in total profit, or about \$4.6 million on average. However, four borrowers, or 7.8 percent, did not have a profit in 1995. These four borrowers owed \$866 million on their outstanding electricity loans as of September 30, 1996. Furthermore, two of these four borrowers had losses in at least 1 year between 1992 and 1994.

Our analysis also showed that, in general, the majority of electricity loan borrowers had other favorable financial ratios. This part of our analysis covered the following measures, which are also discussed below: current ratio, which is a measure of liquidity, and debt-to-asset ratio and times-interest-earned ratio, which are measures of solvency.

Current ratio. This measure shows the extent to which a borrower has sufficient current assets to cover its current liabilities. About 88 percent of the distribution borrowers and 94 percent of the power supply borrowers had current assets that equaled or exceeded their current liabilities. However, 100 distribution borrowers and 3 power suppliers had current ratios of less than 1, indicating that they could not, if necessary, cover their current liabilities with their current assets.

Debt-to-asset ratio. This measure shows the extent to which a borrower has sufficient assets to cover all of its debt. About 93 percent of the distribution borrowers and about 22 percent of the power supply borrowers had ratios in the range of 70 percent or less. However, 51 distribution borrowers and 32 power suppliers had ratios of between 71 percent and 99 percent. Furthermore, two distribution borrowers and eight power suppliers had ratios that exceeded 100 percent, showing that their total debt was greater than their total assets.

Times-interest-earned ratio. This measure shows the ability of a borrower to pay its annual interest expenses. About 96 percent of the distribution borrowers and about 92 percent of the power supply borrowers had 1995 income that equaled or exceeded their 1995 interest expenses. However, the income of 34 distribution borrowers and of 4 power suppliers was less than their 1995 interest expenses, indicating that their ability to cover those expenses as they come due was questionable.

The financial characteristics of electricity loan borrowers at the end of 1992 through 1994 show results similar to the characteristics at the end of 1995. (App. III provides a more detailed analysis of the borrowers' characteristics for 1992 through 1995.)

Telecommunications Loans

RUS' automated files contained financial information for 848 borrowers with outstanding telecommunications loans (direct and/or guaranteed loans) at the end of 1995. On the basis of the measures we used, including net worth and net income, we found that the vast majority, but not all, of these borrowers also had generally favorable financial characteristics. For example, these borrowers had average assets of \$17.7 million, liabilities of \$9.3 million, and a net worth of \$8.4 million. Almost 91 percent of them had a net worth of \$1 million or more. However, three borrowers had total liabilities that exceeded their total assets. These three borrowers owed \$5.4 million on their outstanding telecommunications loans as of September 30, 1996. RUS officials told us that these three borrowers had received loans during 1992 and 1993 to start their telecommunications operations or to rebuild their systems. RUS officials also told us that they anticipate that these borrowers will achieve a positive equity position in late 1997 and 1998 once construction is completed and service to customers is provided.

Another financial characteristic of the borrowers with telecommunications loans is the net income they made in 1995. The telecommunications loan borrowers had average operating revenues of \$6 million, operating expenses of \$4.6 million, and a net operating income of \$1.4 million. Overall, they had a total profit of \$772.6 million and an average profit of slightly more than \$910,000. Twenty-nine percent of the borrowers made more than \$1 million in profit in 1995; these borrowers accounted for 92.5 percent of the total profit. However, 14 borrowers had a loss in 1995. These 14 borrowers owed \$103 million on their outstanding telecommunications loans as of September 30, 1996. Furthermore, 2 of these 14 borrowers had losses in at least 1 year between 1992 and 1994.

Our analysis also showed that, in general, the majority of telecommunications loan borrowers had other favorable financial ratios. This part of our analysis covered the following measures that we previously discussed for the electricity borrowers: current ratio, debt-to-asset ratio, and times-interest-earned ratio.

Current ratio. About 91 percent of the borrowers had current assets that equaled or exceeded current liabilities. However, 73 borrowers had current ratios of less than 1, indicating that they could not, if necessary, cover their current liabilities with their current assets.

Debt-to-asset ratio. About 88 percent of the borrowers had ratios of 70 percent or less. However, 98 borrowers had ratios of between 71 percent and 99 percent, and 3 borrowers had ratios that exceeded 100 percent.

Times-interest-earned ratio. About 98 percent of the borrowers had income that equaled or exceeded their interest expenses. However, the income of 14 borrowers was less than their interest expenses.

As was the case with the electricity loan borrowers, our analysis of the financial characteristics of telecommunications loan borrowers at the end of 1992 through 1994 shows results similar to those at the end of 1995. (App. III also provides a more detailed analysis on the characteristics of the telecommunications loan borrowers for 1992 through 1995.)

Agency Comments

We provided a draft of this report to USDA for its review and comment. USDA provided comments on two areas. First, USDA agreed that RUS has a significant problem with a small number of electricity loan borrowers that are experiencing financial difficulty. USDA stated that much of the problem relates to loans that were made to borrowers many years ago for investments involving nuclear power-generating plants and related transmission facilities. USDA added that RUS and the Department have been working, in some cases in conjunction with the Department of Justice, in an attempt to resolve the agency's problems. Second, USDA stated that the Rural Electrification Loan Restructuring Act of 1993 (P.L. 103-129, Nov. 1, 1993) significantly amended the RUS electricity and telecommunications programs and dramatically reduced their cost to the government. USDA provided a comparison of the total dollar amounts of subsidy costs and loan levels shortly before and after passage of the law. USDA's comments are contained in appendix IV.

We performed our review of RUS' utility loan programs from April 1996 through February 1997 in accordance with generally accepted government auditing standards. Our scope and methodology are discussed in appendix V.

We are sending copies of this report to the appropriate Senate and House committees; interested Members of Congress; the Secretary of Agriculture; the Administrator of RUS; the Director, Office of Management and Budget; and other interested parties. We will also make copies available to others upon request.

Please call me at (202) 512-5138 if you or your staff have any questions. Major contributors to this report are listed in appendix VI.

Sincerely yours,



Robert A. Robinson
Director, Food and
Agriculture Issues

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Abbreviations

FFB	Federal Financing Bank
GAO	General Accounting Office
RDA	Rural Development Administration
REA	Rural Electrification Administration
RTB	Rural Telephone Bank
RUS	Rural Utilities Service
USDA	U.S. Department of Agriculture

Description of RUS' Utility Loan Programs

The Rural Utilities Service (RUS), established by the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act of 1994 (P.L. 103-354, Oct. 13, 1994), administers the electricity and telecommunications programs that were operated by the former Rural Electrification Administration (REA) and the water and waste disposal programs that were operated by the former Rural Development Administration (RDA). Within USDA, RUS is located in the Rural Development mission area. The Rural Electrification Act of 1936, as amended (7 U.S.C. 901 *et seq.*), provides the basic statutory authority for the electricity and telecommunications programs, including the authority for guaranteed loans to be made by the Federal Financing Bank (FFB) of the Treasury. The Consolidated Farm and Rural Development Act, as amended (7 U.S.C. 1921 *et seq.*), contains the authority for the water and waste disposal programs.

This appendix provides information on the different loans within the utility loan programs and on the differences in procedures for making and servicing loans. Information is also provided on the number and dollar amount of loans that RUS made or guaranteed during fiscal years 1992 through 1996 and on RUS' subsidy and administrative costs for operating the utility loan programs during those years. Finally, this appendix describes the credit reform procedures in the Federal Credit Reform Act of 1990.

Utility Loan Programs

The following is a general description of RUS' utility loans.

Electricity loans. RUS makes direct loans primarily to construct and maintain electricity distribution facilities that provide electricity to rural users. RUS also places guarantees on loans made to finance the construction, repair, and improvement of electricity generation and transmission facilities. The following are the types of loans provided in the electricity program:

- Direct loans with a 5 percent interest rate. These loans, referred to as hardship rate loans, are made to borrowers that serve financially distressed rural areas.
- Direct loans with an interest rate that is tied to an index of municipal borrowing rates. These loans, referred to as municipal rate loans, have a maximum interest rate of 7 percent when the borrower meets, at the time of loan approval, either a consumer density test or both a rate disparity test and a consumer income test. To meet the first test, the average

number of consumers per mile of line of the borrower's total electric system has to be less than 5.5. For the rate disparity test, the borrower's average revenue per kilowatt hour sold has to be more than the average revenue per kilowatt hour sold by all electric utilities in the state in which the borrower provides service. For the consumer income test, either the average per capita income of the residents receiving electric service from the borrower has to be less than the average per capita income of the residents of the state in which the borrower provides service or the median household income of the households receiving electric service from the borrower has to be less than the median household income of the households in the state. If these tests are not met, the interest rate may exceed 7 percent.

- Guaranteed loans. RUS places a USDA repayment guarantee on loans made by the FFB; these loans have an interest rate that is the Treasury's cost of money plus one-eighth of 1 percent. If the applicant selects the FFB as the lender, RUS is required to place a 100-percent guarantee on the loan. While RUS can also place a 100-percent USDA guarantee on electricity loans made by commercial lenders, it has not guaranteed any such loans in recent years because all applicants have applied for loans to be made by the FFB.

Telecommunications loans. RUS' direct and guaranteed loans are made primarily to build and improve telephone services and telecommunications facilities in rural areas, including loans for advanced telecommunications facilities and services such as fiber-optic cabling, digital-switching equipment, and educational television applications. RUS' telecommunications loans are the following:

- Direct loans with a 5 percent interest rate. These loans, referred to as hardship rate loans, are made to borrowers that are financially stressed.
- Direct loans with an interest rate that matches USDA's cost of money. These loans are referred to as cost-of-money rate loans.
- Guaranteed loans. RUS places a USDA repayment guarantee on loans made by the FFB, which have an interest rate that is the Treasury's cost of money plus one-eighth of 1 percent. As with electricity loans, if an applicant selects the FFB as the lender, RUS is required to place a 100-percent guarantee on the loan. While RUS can also place a 100-percent USDA guarantee on telecommunications loans made by commercial lenders, it has not guaranteed any such loans in recent years because all applicants have applied for loans to be made by the FFB.

Rural Telephone Bank loans. In administering the Rural Telephone Bank (RTB) loan program, RUS makes direct loans to telephone cooperatives and

commercial companies that receive RUS' telecommunications loans. RTB loans, which have an interest rate that matches RTB's cost of money, are made to extend and improve rural telephone services, including advanced telecommunications facilities and services.

Water and waste disposal loans. RUS' direct and guaranteed water loans are made to improve the storage, treatment, and distribution of water in rural areas. Similarly, RUS' direct and guaranteed waste disposal loans are made to collect, treat, and dispose of waste, including loans for sewer systems, solid waste disposal, and storm drainage. Other than the purpose of the loan, there are no differences between RUS' water and waste disposal loans. The loans fall into the following categories:

- Direct loans with a 4.5 percent interest rate. These loans, referred to as poverty-rate loans, are made to borrowers that serve areas where the median household income is below the poverty line or is less than 80 percent of a state's nonmetropolitan median household income. To receive a loan with this interest rate, the borrower's project has to address health or sanitary violations identified by the state's health department. The maximum interest rate authorized on a poverty-rate loan is 5 percent.
- Direct loans with an interest rate that is tied to an index of municipal tax-exempt bonds. These loans, referred to as market-rate loans, are made to borrowers that serve areas where the median household income exceeds a state's nonmetropolitan median household income.
- Direct loans with an interest rate that is one-half the difference between the rates on poverty- and market-rate loans. These loans, referred to as intermediate-rate loans, are made to borrowers that serve areas where the median household income is between 80 percent and 100 percent of a state's nonmetropolitan median household income. Loans at this rate are also made to borrowers that serve areas where the median income is less than 80 percent of a state's nonmetropolitan median household income but where the state's health department has not identified a health or sanitary problem. The maximum interest rate authorized on an intermediate-rate loan is 7 percent.
- Guaranteed loans. RUS places a USDA repayment guarantee on loans made by commercial lenders; these loans have an interest rate that is agreed upon by the lender and the borrower. While RUS can place a maximum guarantee of 90 percent on these loans, in most cases it has placed an 80-percent guarantee.

Loan Making and Servicing

The Assistant Administrators for RUS' electricity, telecommunications, and water and waste disposal programs provide direction and guidance on their respective programs for loan making and servicing. The Assistant Administrators also review and approve certain loan applications.

Many loan-making and -servicing functions associated with electricity and telecommunications loans are centralized at RUS' headquarters. RUS' regional offices in the electricity program and area offices in the telecommunications program process loan applications, decide on the technical aspects and the financial feasibility of the proposed projects, and service approved loans. Also, the Power Supply Division in the electricity program services those borrowers that have guaranteed loans for electricity generation and transmission purposes. Staff assigned to the regional and area offices and to the Power Supply Division are physically located at RUS' headquarters in Washington, D.C.

RUS also employs approximately 70 general field representatives who are located throughout the country; about half of these work on the electricity program and the other half on the telecommunications program. These field representatives are an extension of the headquarters-based regional and area office staff. For example, during the loan-making process, they assist an applicant by, among other things, providing advice on the application process and documentation requirements. During loan-servicing, they monitor project construction. While most of their oversight is performed by reviewing the documents that borrowers have submitted, the field representatives also visit, at least once a year, project sites to determine their status.

RUS also employs about 35 field accountants who conduct financial reviews of electricity and telecommunications loan borrowers. Among other things, these accountants perform fiscal reviews to determine if funds are used properly and if adequate records of expenditures are maintained.

In contrast, many loan-making and -servicing functions associated with water and waste disposal loans are managed by staff physically located in field offices. Specifically, staff in the Rural Development mission area who are in state, district, or other field offices process water and waste disposal loan applications, decide on the technical aspects and the financial feasibility of the proposed projects, and service approved loans.

The programs also differ in the servicing of guaranteed loans. Specifically, RUS staff service the electricity and telecommunications loans made by the FFB that have USDA guarantees. Servicing includes billings, loan payment collections, and visits and contacts with borrowers. On the other hand, commercial lenders service the guaranteed water and waste disposal loans that they made. RUS periodically monitors the lenders to ensure that they are servicing the accounts.

Loans Made and Guaranteed in RUS' Utility Loan Programs

Tables I.1 through I.3 contain information on the number and dollar amount of loans that RUS made or guaranteed during fiscal years 1992 through 1996 on the various utility loan programs. For example, table I.1 shows that the overwhelming number of loans made each year in each of the programs were direct loans. Table I.2 shows that approximately \$2 billion in loans was made in each year over the 5-year period. Table I.3 shows that the average amount of all guaranteed loans was far greater than the average amount of all direct loans. All of the electricity and telecommunications loans that RUS guaranteed during this 5-year period were made by Treasury's FFB; all RUS-guaranteed water and waste disposal loans were made by commercial lenders.

Appendix I
Description of RUS' Utility Loan Programs

Table I.1: Number of Utility Loans Made or Guaranteed by RUS, Fiscal Years 1992-96

Program and loan type	1992	1993	1994	1995	1996	Total
Electricity						
Direct standard rate	193	256	a	a	a	449
Direct hardship rate	a	a	29	22	23	74
Direct municipal rate	a	a	111	105	96	312
Subtotal direct	193	256	140	127	119	835
Guaranteed	14	3	9	8	11	45
Total	207	259	149	135	130	880
Telecommunications						
Direct standard rate	40	43	a	a	a	83
Direct hardship rate	a	a	18	8	12	38
Direct cost-of-money rate	a	a	50	48	44	142
Subtotal direct	40	43	68	56	56	263
Guaranteed	3	7	10	12	6	38
Total	43	50	78	68	62	301
Rural Telephone Bank						
Direct	29	38	50	48	44	209
Water and waste disposal						
Direct poverty rate	355	433	412	456	431	2,087
Direct intermediate rate	378	422	506	511	412	2,229
Direct market rate	126	72	75	85	52	410
Subtotal direct	859	927	993	1,052	895	4,726
Guaranteed	12	5	8	b	13	38
Total	871	932	1,001	1,052	908	4,764
RUS total						
Direct	1,121	1,264	1,251	1,283	1,114	6,033
Guaranteed	29	15	27	20	30	121
Total	1,150	1,279	1,278	1,303	1,144	6,154

^aUSDA's direct loans for fiscal years 1992 and 1993 were made at a 5 percent interest rate and were referred to as standard rate REA loans. USDA was authorized in a November 1993 amendment to the Rural Electrification Act to make direct hardship rate, municipal rate, and cost-of-money rate loans starting in fiscal year 1994.

^bUSDA's appropriation for fiscal year 1995 did not authorize the Department to guarantee water and waste disposal loans.

Sources: USDA, Budget Explanatory Notes for Committee on Appropriations, fiscal years 1994 through 1997, and RUS' reports.

Appendix I
Description of RUS' Utility Loan Programs

Table I.2: Total Dollar Amount of Utility Loans Made or Guaranteed by RUS, Fiscal Years 1992-96

Program and loan type	1992	1993	1994	1995	1996	Total
Electricity						
Direct standard rate	\$622.1	\$913.4	a	a	a	\$1,535.5
Direct hardship rate	a	a	\$109.2	\$74.1	\$90.6	273.9
Direct municipal rate	a	a	408.8	536.4	544.6	1,489.8
Subtotal direct	622.1	913.4	518.0	610.5	635.2	3,299.1
Guaranteed	182.8	113.3	269.8	300.0	187.3	1,053.3
Total	\$804.9	\$1,026.7	\$787.8	\$910.5	\$822.5	\$4,352.4
Telecommunications						
Direct standard rate	204.5	311.0	a	a	a	515.5
Direct hardship rate	a	a	70.3	48.1	71.2	189.6
Direct cost-of-money rate	a	a	198.0	242.3	216.7	657.1
Subtotal direct	204.5	311.0	268.3	290.5	287.9	1,362.3
Guaranteed	35.2	67.1	59.7	119.4	78.1	359.6
Total	\$239.7	\$378.1	\$328.1	\$409.9	\$366.0	\$1,721.8
Rural Telephone Bank						
Direct	177.0	175.0	199.8	175.0	126.4	853.3
Water and waste disposal						
Direct poverty rate	217.9	319.6	282.6	328.2	291.5	1,439.8
Direct intermediate rate	261.9	268.6	372.0	411.4	272.6	1,586.4
Direct market rate	120.2	59.0	60.9	88.3	39.1	367.6
Subtotal direct	600.0	647.1	715.5	827.9	603.2	3,393.8
Guaranteed	4.6	1.7	5.2	b	59.1	70.5
Total	\$604.6	\$648.8	\$720.7	\$827.9	\$662.3	\$3,464.3
RUS total						
Direct	\$1,603.6	\$2,046.5	\$1,701.7	\$1,903.9	\$1,652.8	\$8,908.4
Guaranteed	\$222.7	\$182.1	\$334.7	\$419.4	\$324.5	\$1,483.3
Total	\$1,826.2	\$2,228.6	\$2,036.4	\$2,323.3	\$1,977.3	\$10,391.8

Note: Subtotals and totals may not add due to rounding.

^aUSDA's direct loans for fiscal years 1992 and 1993 were made at a 5 percent interest rate and were referred to as standard rate REA loans. USDA was authorized in a November 1993 amendment to the Rural Electrification Act to make direct hardship rate, municipal rate, and cost-of-money rate loans starting in fiscal year 1994.

^bUSDA's appropriation for fiscal year 1995 did not authorize the Department to guarantee water and waste disposal loans.

Sources: USDA, Budget Explanatory Notes for Committee on Appropriations, fiscal years 1994 through 1997, and RUS' reports.

Appendix I
Description of RUS' Utility Loan Programs

Table I.3: Average Dollar Amount of Utility Loans Made or Guaranteed by RUS, Fiscal Years 1992-96

Dollars in millions

Program and loan type	1992	1993	1994	1995	1996	5-year average
Electricity						
Direct standard rate	\$3.2	\$3.6	a	a	a	\$3.4
Direct hardship rate	a	a	\$3.8	\$3.4	\$3.9	3.7
Direct municipal rate	a	a	3.7	5.1	5.7	4.8
All direct	3.2	3.6	3.7	4.8	5.3	4.0
Guaranteed	13.1	37.8	30.0	37.5	17.0	23.4
Average for all electricity	3.9	4.0	5.3	6.7	6.3	4.9
Telecommunications						
Direct standard rate	5.1	7.2	a	a	a	6.2
Direct hardship rate	a	a	3.9	6.0	5.9	5.0
Direct cost-of-money rate	a	a	4.0	5.0	4.9	4.6
All direct	5.1	7.2	3.9	5.2	5.1	5.2
Guaranteed	11.7	9.6	6.0	10.0	13.0	9.5
Average for all telecommunications	5.6	7.6	4.2	6.0	5.9	5.7
Rural Telephone Bank						
Direct	6.1	4.6	4.0	3.6	2.9	4.1
Water and waste disposal						
Direct poverty rate	0.6	0.7	0.7	0.7	0.7	0.7
Direct intermediate rate	0.7	0.6	0.7	0.8	0.7	0.7
Direct market rate	1.0	0.8	0.8	1.0	0.8	0.9
All direct	0.7	0.7	0.7	0.8	0.7	0.7
Guaranteed	0.4	0.3	0.6	b	4.5	1.9
Average for all water and waste disposal	0.7	0.7	0.7	0.8	0.7	0.7
All RUS loans						
Average for all direct	1.4	1.6	1.4	1.5	1.5	1.5
Average for all guaranteed	7.7	12.1	12.4	21.0	10.8	12.3
Average for all loans	1.6	1.7	1.6	1.8	1.7	1.7

^aUSDA's direct loans for fiscal years 1992 and 1993 were made at a 5 percent interest rate and were referred to as standard rate REA loans. USDA was authorized in a November 1993 amendment to the Rural Electrification Act to make direct hardship rate, municipal rate, and cost-of-money rate loans starting in fiscal year 1994.

^bUSDA's appropriation for fiscal year 1995 did not authorize the Department to guarantee water and waste disposal loans.

Source: GAO's calculation.

RUS' Costs for the Utility Loan Programs

Tables I.4 through I.6 contain information on RUS' subsidy costs for making and guaranteeing utility program loans and its administrative costs for operating the utility loan programs during fiscal years 1992 through 1996. For example, table I.4 shows that the subsidy costs for direct loans in the programs in each year were considerably higher than for guaranteed loans. Table I.5 shows that RUS' administrative costs for each program were fairly consistent in each year—in the mid-\$60 million to mid-\$70 million range. Table I.6 shows that RUS' total costs were approximately \$300 million in each year.

Appendix I
Description of RUS' Utility Loan Programs

Table I.4: RUS' Subsidy Costs for Utility Loans, Fiscal Years 1992-96

Dollars in millions

Program and loan type	1992	1993	1994	1995	1996	Total
Electricity						
Direct standard rate	\$117.1	\$117.3	a	a	a	\$234.4
Direct hardship rate	a	a	\$18.7	\$9.7	\$21.2	49.6
Direct municipal rate	a	a	46.0	46.0	56.9	148.9
Subtotal direct	117.1	117.3	64.7	55.7	78.1	432.9
Guaranteed	3.3	5.3	3.1	0	1.6	13.3
Total	\$120.4	\$122.6	\$67.8	\$55.7	\$79.7	\$446.2
Telecommunications						
Direct standard rate	34.4	36.3	a	a	a	70.7
Direct hardship rate	a	a	11.3	3.8	13.9	29.0
Direct cost-of-money rate	a	a	<0.1	0.1	<0.1	0.1
Subtotal direct	34.4	36.3	11.3	3.9	13.9	99.8
Guaranteed	0	0.1	0	0	0	0.1
Total	\$34.4	\$36.3	\$11.3	\$3.9	\$13.9	\$99.9
Rural Telephone Bank						
Direct	3.6	<0.1	0.8	0.8	3.2	8.4
Water and waste disposal						
Direct ^b	84.6	82.1	115.8	126.5	135.7	544.7
Guaranteed	0	0	0	c	0	0
Total	\$84.6	\$82.1	\$115.8	\$126.5	\$135.7	\$544.7
RUS total						
Direct	\$239.7	\$235.8	\$192.6	\$186.9	\$230.9	\$1,085.9
Guaranteed	\$ 3.3	\$ 5.4	\$ 3.1	\$ 0	\$ 1.6	\$ 13.3
Total	\$243.0	\$241.1	\$195.7	\$186.9	\$232.5	\$1,099.2

Note: Totals may not add due to rounding.

^aUSDA's direct loans for fiscal years 1992 and 1993 were made at a 5 percent interest rate and were referred to as standard rate REA loans. USDA was authorized in a November 1993 amendment to the Rural Electrification Act to make direct hardship rate, municipal rate, and cost-of-money rate loans starting in fiscal year 1994.

^bAccording to officials in the Budget Division of USDA's Rural Development mission area, a breakout of the subsidy costs for the three types of direct water and waste disposal loans—poverty rate, intermediate rate, and market rate—is not available because the Budget Division's subsidy cost records are not maintained by the type of loan.

^cUSDA's appropriation for fiscal year 1995 did not authorize the Department to guarantee water and waste disposal loans.

Sources: Obligation data obtained from USDA, Budget Explanatory Notes for Committee on Appropriations, fiscal years 1994 through 1997, and information provided to GAO by the Budget Division in USDA's Rural Development mission area.

Appendix I
Description of RUS' Utility Loan Programs

Table I.5: RUS' Administrative Costs for the Utility Loan Programs, Fiscal Years 1992-96

Dollars in millions						
Program	1992	1993	1994	1995	1996	Total
Electricity	\$20.8	\$20.8	\$21.2	\$21.2	\$21.2	\$105.1
Telecommunications	8.6	8.6	8.8	8.8	8.8	43.6
Rural Telephone Bank	8.6	8.6	8.8	8.8	3.5	38.4
Water and waste disposal	26.8	28.4	34.3	34.4	31.1	154.9
Total	\$64.9	\$66.5	\$73.0	\$73.1	\$64.6	\$342.1

Note: RUS' administrative costs apply to the operation of both direct and guaranteed loans in the various utility loan programs. The amounts shown do not include any administrative costs that Treasury's FFB or commercial lenders may have incurred on RUS-guaranteed loans. Totals may not add due to rounding.

Source: Information provided to GAO by the Budget Division in USDA's Rural Development mission area.

Table I.6: RUS' Total Costs for the Utility Loan Programs, Fiscal Years 1992-96

Dollars in millions						
Program	1992	1993	1994	1995	1996	Total
Electricity	\$141.1	\$143.4	\$ 89.0	\$ 76.9	\$100.9	\$ 551.3
Telecommunications	43.1	45.0	20.1	12.7	22.7	143.5
Rural Telephone Bank	12.3	8.7	9.6	9.6	6.7	46.8
Water and waste disposal	111.4	110.6	150.0	160.9	166.8	699.7
Total	\$307.9	\$307.6	\$268.7	\$260.0	\$297.1	\$1,441.3

Note: Totals may not add due to rounding.

Source: GAO's calculation.

Credit Reform

The two key principles of credit reform contained in the Federal Credit Reform Act of 1990 center on the (1) definition of cost in terms of the present value of the estimated cash flow over the life of a credit instrument and (2) inclusion in the budget of the costs of credit programs before direct or guaranteed loans are made or modified.

Credit reform requirements separate the government's cost of extending or guaranteeing credit, called the subsidy cost, from administrative and unsubsidized program costs. Administrative expenses receive separate appropriations. They are treated on a cash basis and reported separately in

the budget. The unsubsidized portion of a direct loan or loan guarantee is expected to be recovered from the borrower.

The Credit Reform Act defines the subsidy cost of direct loans as the present value—over the loan's life—of estimated disbursements by the government (loan disbursements and other payments) minus estimated payments to the government (repayments of principal, payments of interest, and other payments) after adjusting for projected defaults, prepayments, fees, penalties, and other recoveries. It defines the subsidy cost of loan guarantees as the present value of cash flows from estimated payments by the government (for defaults and delinquencies, interest rate subsidies, and other payments) minus estimated payments to the government (for loan origination and other fees, penalties, and recoveries). Permanent, indefinite appropriations are available should the appropriated subsidy cost be less than the estimates in a later fiscal year.

Before credit reform, credit programs—like other programs—were reported in the budget on a cash basis. As a result, it was difficult to make appropriate cost comparisons between direct loan and loan guarantee programs and between credit and noncredit programs. Credit programs had different economic effects than most budget outlays, such as the purchase of goods and services, income transfers, and grants. In the case of direct loans, for example, the fact that the loan recipient was obligated to repay the government over time meant that the budgetary impact of a direct loan disbursement could be much less than other budget transactions of the same dollar amount. This lower budgetary impact also created a bias in favor of loan guarantees over direct loans. Loan guarantees appeared to be free, while direct loans appeared to be expensive because the budget did not recognize that at least some of the loan guarantees would default and that some of the direct loans would be repaid.

The Credit Reform Act changed this treatment for direct loans and loan guarantees made on or after October 1, 1991.

Financial Condition of RUS' Utility Loan Portfolios

This appendix contains information on the amount of outstanding principal owed on RUS' electricity, telecommunications, and water and waste disposal loans, and the portions owed by delinquent borrowers, at the end of fiscal years 1992 through 1996. For example, table II.1 shows that the amount of outstanding principal owed on electricity loans declined by about \$2.1 billion, or 6.2 percent, from the end of fiscal year 1992 to the end of fiscal year 1996. Table II.2 shows that the amount of outstanding principal owed on telecommunications loans declined by about \$168 million, or 3.1 percent, over the same period. On the other hand, table II.3 shows that the outstanding principal owed on water and waste loans increased by about \$1.5 billion, or 40.6 percent, over this period.

Appendix II
Financial Condition of RUS' Utility Loan
Portfolios

Table II.1: Amount of Outstanding Principal Owed on Electricity Loans Made or Guaranteed by RUS, and Portion Owed by Delinquent Borrowers, September 30, 1992, Through September 30, 1996

Dollars in millions					
Loan type	1992	1993	1994	1995	1996
RUS' direct loans					
Outstanding principal owed by all borrowers	\$11,978.4	\$11,855.8	\$11,771.3	\$11,894.8	\$11,475.2
Outstanding principal owed by delinquent borrowers	92.2	92.2	29.6	29.6	29.6
Guaranteed FFB loans					
Outstanding principal owed by all borrowers	14,676.6	14,249.3	13,789.1	13,780.4	13,328.6
Outstanding principal owed by delinquent borrowers	765.5	739.0	591.6	584.5	572.0
Other guaranteed loans					
Outstanding principal owed by all borrowers	755.4	936.8	702.6	685.2	664.7
Outstanding principal owed by delinquent borrowers	0	16.9	16.7	16.5	16.3
Restructured loans^a					
Outstanding principal owed by all borrowers	7,027.3	7,179.8	8,172.0	8,008.3	6,841.1
Outstanding principal owed by delinquent borrowers	0	0	0	0	0
Total loans					
Outstanding principal owed by all borrowers	\$34,437.7	\$34,221.7	\$34,435.0	\$34,368.7	\$32,309.6
Outstanding principal owed by delinquent borrowers	\$857.7	\$848.1	\$637.9	\$630.6	\$617.9

Note: The information in this table, and in tables II.2 and II.3, covers outstanding principal on loans made or guaranteed by RUS. We have not adjusted the outstanding loan amounts to reflect the allowance for losses that RUS includes in its financial statements or the adequacy of reserves on the loans.

^aIncludes previously issued (1) direct loans made by RUS, (2) guaranteed loans made by the FFB, (3) guaranteed loans made by commercial lenders on which RUS agreed to be directly liable for repaying the loan, and (4) loans that had been owed by borrowers now assumed by other utilities. The amounts cover the principal and the capitalized interest owed on the loans. The loans in this category are not included in the other direct and guaranteed loan categories.

Source: RUS' reports.

Appendix II
Financial Condition of RUS' Utility Loan
Portfolios

Table II.2: Amount of Outstanding Principal Owed on Telecommunications Loans Made or Guaranteed by RUS, September 30, 1992, Through September 30, 1996

Dollars in millions					
Loan type	1992	1993	1994	1995	1996
RUS' direct loans	\$3,251.9	\$3,306.5	\$3,320.2	\$3,369.0	\$3,360.9
Guaranteed FFB loans	352.1	340.8	297.0	304.3	318.4
Other guaranteed loans	2.4	2.3	2.2	2.1	1.9
RTB's direct loans	1,727.3	1,733.9	1,543.0	1,531.7	1,484.9
Total loans	\$5,333.7	\$5,383.5	\$5,162.4	\$5,207.1	\$5,166.1

Note: There were no delinquent telecommunications loans at the end of fiscal years 1992 through 1996. We do not include as delinquent those borrowers that are shown in RUS' reports as being past due on repayments at the end of the fiscal years when the delinquency was due to billing, payment, or administrative errors and when the past due amount was paid shortly after the start of the next fiscal year.

Source: RUS' reports.

Table II.3: Amount of Outstanding Principal Owed on Water and Waste Disposal Loans Made or Guaranteed by RUS, and Portion Owed by Delinquent Borrowers, September 30, 1992, Through September 30, 1996

Dollars in millions					
Loan type	1992	1993	1994	1995	1996
Direct loans					
Outstanding principal owed by all borrowers	\$3,580.1	\$3,848.5	\$4,113.0	\$4,511.5	\$5,024.9
Outstanding principal owed by delinquent borrowers	53.7	29.6	50.5	39.5	43.3
Guaranteed loans					
Outstanding principal owed by all borrowers	0	0.9	4.7	7.1	7.9
Outstanding principal owed by delinquent borrowers	0	0	0	0	0
Total loans					
Outstanding principal owed by all borrowers	\$3,580.1	\$3,849.4	\$4,117.7	\$4,518.6	\$5,032.8
Outstanding principal owed by delinquent borrowers	\$53.7	\$29.6	\$50.5	\$39.5	\$43.3

Source: RUS' reports.

Financial Information on Borrowers With Electricity and Telecommunications Loans

This appendix contains information on the financial characteristics of borrowers that had RUS' electricity and telecommunications loans and that reported financial information to RUS as of the end of calendar years 1992 through 1995.¹ A glossary is also provided that defines the financial measures used to describe these borrowers.

Financial Characteristics of Borrowers With RUS' Electricity and Telecommunications Loans

Tables III.1 through III.9 provide information describing the financial characteristics of electricity and telecommunications loan borrowers that reported to RUS. The first three tables provide information on the distribution borrowers with electricity loans. The second set of three tables provides information on the power supply borrowers with electricity loans. The last three tables provide information on borrowers with telecommunications loans.

Tables III.1, III.4, and III.7 show that the overwhelming majority of the borrowers had a net worth of \$1 million or more at the end of each year from 1992 through 1995. Tables III.2, III.5, and III.8 show that most of them had profits of at least \$100,000 in each of these years. Tables III.3, III.6, and III.9 show that the current ratios, debt-to-asset ratios, and times-interest-earned ratios of the borrowers were generally favorable in each year.

¹The information presented in this appendix was taken from RUS' databases. The information we present covers more borrowers than are covered in RUS' annual statistical reports on borrowers, which exclude, for example, borrowers that submitted information to the agency after the submission date for publishing the annual reports. However, the information submitted after that date is maintained in the agency's databases.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Table III.1: Number and Percentage of RUS' Electricity Loan Distribution Borrowers, by Range of Net Worth, December 31, 1992, Through December 31, 1995

Range of net worth	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$100 million or more	2	0.2	7	0.8	7	0.8	9	1.1
\$10 million to \$99.9 million	403	46.7	421	49.2	432	51.9	431	53.6
\$1 million to \$9.9 million	447	51.8	419	49.0	385	46.3	359	44.7
\$100,000 to \$999,999	7	0.8	4	0.5	4	0.5	2	0.2
\$0 to \$99,999	1	0.1	1	0.1	1	0.1	1	0.1
Less than \$0	3	0.3	3	0.4	3	0.4	2	0.2
Total	863	100.0^a	855	100.0	832	100.0	804	100.0^a

^aDoes not add due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Table III.2: Number and Percentage of RUS' Electricity Loan Distribution Borrowers, by Range of Profit, December 31, 1992, Through December 31, 1995

Range of profit	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$10 million or more	4	0.5	6	0.7	4	0.5	4	0.5
\$1 million to \$9.9 million	290	33.6	360	42.1	304	36.5	303	37.7
\$100,000 to \$999,999	512	59.3	459	53.7	478	57.5	438	54.5
\$0 to \$99,999	36	4.2	20	2.3	26	3.1	25	3.1
Less than \$0	21	2.4	10	1.2	20	2.4	34	4.2
Total	863	100.0	855	100.0	832	100.0	804	100.0

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Table III.3: Number and Percentage of RUS' Electricity Loan Distribution Borrowers, by Range of Three Ratio Measures, December 31, 1992, Through December 31, 1995

Ratio measure and range	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
Current ratio								
Five or more times	115	13.3	98	11.5	86	10.3	84	10.4
Two to up to five times	372	43.1	354	41.4	340	40.9	310	38.6
Up to two times	301	34.9	309	36.1	290	34.9	310	38.6
Less than one time	75	8.7	94	11.0	116	13.9	100	12.4
Debt-to-asset ratio								
40 percent or less	92	10.7	100	11.7	101	12.1	94	11.7
41 to 70 percent	660	76.5	685	80.1	674	81.0	657	81.7
71 to 99 percent	108	12.5	67	7.8	54	6.5	51	6.3
100 percent or more	3	0.3	3	0.4	3	0.4	2	0.2
Times-interest-earned ratio								
Five or more times	54	6.3	91	10.6	70	8.4	63	7.8
Two to up to five times	497	57.6	573	67.0	504	60.6	479	59.6
Up to two times	291	33.7	181	21.2	238	28.6	228	28.4
Less than one time	21	2.4	10	1.2	20	2.4	34	4.2

Note: Percentage of borrowers for each ratio may not add to 100.0 percent due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Table III.4: Number and Percentage of RUS' Electricity Loan Power Supply Borrowers, by Range of Net Worth, December 31, 1992, Through December 31, 1995

Range of net worth	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$100 million or more	6	11.1	7	13.0	7	13.0	7	13.7
\$10 million to \$99.9 million	30	55.6	30	55.6	31	57.4	30	58.8
\$1 million to \$9.9 million	4	7.4	4	7.4	3	5.6	5	9.8
\$100,000 to \$999,999	1	1.9	1	1.9	1	1.9	1	2.0
\$0 to \$99,999	0	0	0	0	1	1.9	0	0
Less than \$0	13	24.1	12	22.2	11	20.4	8	15.7
Total	54	100.0	54	100.0^a	54	100.0^a	51	100.0

^aDoes not add due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Table III.5: Number and Percentage of RUS' Electricity Loan Power Supply Borrowers, by Range of Profit, December 31, 1992, Through December 31, 1995

Range of profit	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$10 million or more	10	18.5	7	13.0	7	13.0	9	17.6
\$1 million to \$9.9 million	23	42.6	32	59.3	34	63.0	27	52.9
\$100,000 to \$999,999	10	18.5	5	9.3	4	7.4	8	15.7
\$0 to \$99,999	5	9.3	4	7.4	3	5.6	3	5.9
Less than \$0	6	11.1	6	11.1	6	11.1	4	7.8
Total	54	100.0	54	100.0^a	54	100.0^a	51	100.0^a

^aDoes not add due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Table III.6: Number and Percentage of RUS' Electricity Loan Power Supply Borrowers, by Range of Three Ratio Measures, December 31, 1992, Through December 31, 1995

Ratio measure and range	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
Current ratio								
Five or more times	13	24.1	6	11.1	5	9.3	3	5.9
Two to up to five times	24	44.4	26	48.1	29	53.7	28	54.9
Up to two times	14	25.9	18	33.3	15	27.8	17	33.3
Less than one time	3	5.6	4	7.4	5	9.3	3	5.9
Debt-to-asset ratio								
40 percent or less	0	0	0	0	0	0	0	0
41 to 70 percent	8	14.8	9	16.7	12	22.2	11	21.6
71 to 99 percent	33	61.1	33	61.1	30	55.6	32	62.7
100 percent or more	13	24.1	12	22.2	12	22.2	8	15.7
Times-interest-earned ratio								
Five or more times	1	1.9	1	1.9	0	0	3	5.9
Two to up to five times	6	11.1	11	20.4	6	11.1	6	11.8
Up to two times	41	75.9	36	66.7	42	77.8	38	74.5
Less than one time	6	11.1	6	11.1	6	11.1	4	7.8

Note: Percentage of borrowers for each ratio may not add to 100.0 percent due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by electricity loan borrowers.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Table III.7: Number and Percentage of RUS' Telecommunications Loan Borrowers, by Range of Net Worth, December 31, 1992, Through December 31, 1995

Range of net worth	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$100 million or more	11	1.2	7	0.8	8	0.9	4	0.5
\$10 million to \$99.9 million	148	16.3	154	17.3	158	18.0	172	20.3
\$1 million to \$9.9 million	603	66.3	607	68.2	608	69.3	593	69.9
\$100,000 to \$999,999	142	15.6	118	13.3	100	11.4	76	9.0
\$0 to \$99,999	6	0.7	4	0.4	1	0.1	0	0
Less than \$0	0	0	0	0	2	0.2	3	0.4
Total	910	100.0^a	890	100.0	877	100.0^a	848	100.0^a

^aDoes not add due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by telecommunications loan borrowers.

Table III.8: Number and Percentage of RUS' Telecommunications Loan Borrowers, by Range of Profit, December 31, 1992, Through December 31, 1995

Range of profit	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
\$10 million or more	21	2.3	11	1.2	16	1.8	6	0.7
\$1 million to \$9.9 million	225	24.7	213	23.9	228	26.0	240	28.3
\$100,000 to \$999,999	553	60.8	565	63.5	555	63.3	530	62.5
\$0 to \$99,999	100	11.0	82	9.2	68	7.8	58	6.8
Less than \$0	11	1.2	19	2.1	10	1.1	14	1.7
Total	910	100.0	890	100.0^a	877	100.0	848	100.0

^aDoes not add due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by telecommunications loan borrowers.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Table III.9: Number and Percentage of RUS' Telecommunications Loan Borrowers, by Range of Three Ratio Measures, December 31, 1992, Through December 31, 1995

Ratio measure and range	1992		1993		1994		1995	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
Current ratio								
Five or more times	359	39.5	288	32.4	299	34.1	296	34.9
Two to up to five times	341	37.5	377	42.4	375	42.8	344	40.6
Up to two times	123	13.5	137	15.4	132	15.1	135	15.9
Less than one time	87	9.6	88	9.9	71	8.1	73	8.6
Debt-to-asset ratio								
40 percent or less	179	19.7	197	22.1	218	24.9	244	28.8
41 to 70 percent	567	62.3	552	62.0	528	60.2	503	59.3
71 to 99 percent	164	18.0	141	15.8	129	14.7	98	11.6
100 percent or more	0	0	0	0	2	0.2	3	0.4
Times-interest-earned ratio								
Five or more times	369	40.5	366	41.1	375	42.8	364	42.9
Two to up to five times	446	49.0	421	47.3	422	48.1	392	46.2
Up to two times	84	9.2	84	9.4	70	8.0	78	9.2
Less than one time	11	1.2	19	2.1	10	1.1	14	1.7

Note: Percentage of borrowers for each ratio may not add to 100.0 percent due to rounding.

Source: GAO's analysis of RUS' automated database containing financial information submitted by telecommunications loan borrowers.

Definitions of Financial Statistics for RUS' Borrowers

The following is a general description of the measures used to describe the financial characteristics of RUS' borrowers.

Total assets. Includes current assets (e.g., cash and equivalents), investments, net plants (e.g., plants in service and under construction, less accumulated depreciation), and other noncurrent assets and/or property.

Total liabilities. Includes current liabilities, long-term debt, and other noncurrent liabilities and/or deferred credits.

Total equity or net worth. Includes capital stock and/or patronage capital, memberships, and capital credits.

Operating revenues. Revenues from operations.

Appendix III
Financial Information on Borrowers With
Electricity and Telecommunications Loans

Total operating expenses. Expenses from operations. These expenses include, for example, for power supply borrowers with electricity loans, the costs of producing electricity and/or purchasing power, transmission and distribution expenses, and maintenance expenses. For distribution borrowers with electricity loans, this includes the costs of acquiring power and distribution operating and maintenance expenses. For borrowers with telecommunications loans, this includes plant and nonplant specific operating expenses.

Net operating income. Operating revenues less total operating expenses.

Total net income (profit or loss). Includes operating income plus nonoperating income and/or capital credits less fixed charges (e.g., interest on funded debt and other interest expense).

Current ratio. The ratio is used to measure the extent to which current assets, if liquidated, would cover current liabilities. It is computed by dividing current assets by current liabilities.

Debt-to-asset ratio. The ratio is used to measure the proportion of assets that are financed by debt. It is computed by dividing total debt by total assets.

Times-interest-earned ratio. The ratio is used to measure the extent to which interest on debt can be paid by net income. It is computed by dividing the sum of total net income and interest on debt by interest on debt.

Comments From the U.S. Department of Agriculture



DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

MAR 21 1997

Mr. Robert A. Robinson
Director
Food and Agriculture Issues
Resources, Community, and
Economic Development Division
General Accounting Office
441 G Street, NW
Washington, D.C. 20548

Dear Mr. Robinson:

We appreciate the opportunity to review and comment on the draft General Accounting Office (GAO) report entitled Rural Development: Financial Condition of the Rural Utilities Service's Loan Portfolio. We understand this report is for the Chairman of the House Budget Committee.

There are two items we would like to bring to your attention. First, as the report correctly indicates, there are a small number of borrowers in the RUS electric program who are experiencing financial difficulty. For the most part, these are power supply borrowers who, in the late 1970's and early 1980's, made investments in nuclear power generating plants and related transmission facilities, usually in participation with investor-owned electric utilities. These investments were made during a period of rapidly increasing construction and material costs, changing environmental regulations, and soaring interest rates. Concurrent with these higher costs, projected demand for energy, in many cases, did not materialize. This resulted in some borrowers experiencing debt repayment problems.

Since President Clinton appointed Mr. Beyer as Administrator of RUS, USDA has made every effort to work through these problems. Where necessary, this has included working with the Department of Justice to resolve serious debt situations. USDA has an obligation to manage the RUS loan portfolio in the best interests of the taxpayer and to that end will continue to aggressively seek solutions that result in maximizing recovery of Federal loan funds.

Appendix IV
Comments From the U.S. Department of
Agriculture

Mr. Robert A. Robinson

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Second, the Congress recently examined the RUS electric and telecommunications loan programs and passed the Rural Electrification Loan Restructuring Act of 1993 (RELRA). This was signed into law by President Clinton on November 1, 1993. The RELRA significantly amended the RUS electric and telecommunications programs and dramatically reduced their cost to the Government.

For example, during the period covered by this report, the interest subsidy costs for electric loans approved in 1992 and 1993 (pre-RELRA) totaled \$243 million. This provided for a total loan and guarantee level of \$1,831.6 million. For 1994-96, (post-RELRA), the interest subsidy required for a loan level of \$2,520.8 million, \$689.2 million more than the 1992-93 period, was \$203.2 million, a decrease of \$39.8 million or 16.4 percent.

In the telecommunications program during the same period, the 1992-93 interest subsidy totaled \$70.7 million, which provided a loan and guarantee level of \$969.8 million. Post-RELRA, 1994-96, the interest subsidy of \$29.1 million, a decrease of \$40.6 million, or 59 percent, provided for a loan and guarantee level of \$1,605.2 million, an increase of \$635.4 million, or 65.5 percent.

Again, we appreciate the opportunity to comment on this draft report.

Sincerely,



JILL LONG THOMPSON
Under Secretary
Rural Development

Objectives, Scope, and Methodology

This appendix contains information on our objectives, scope, and methodology in conducting this review. In April 1996, we initiated a survey of RUS' loan portfolios. Subsequently, on October 17, 1996, the Chairman of the Committee on the Budget, House of Representatives, wrote to us expressing his concern about the financial risks associated with RUS' lending and asking that we report to him on the (1) financial condition of the electricity, telecommunications, and water and waste disposal loan portfolios and (2) financial characteristics of borrowers having electricity and telecommunications loans.

In conducting our review, we focused on the financial condition of RUS' loan portfolios at the end of fiscal year 1996 and, for trend information, the preceding 4 fiscal years. For the financial characteristics of the electricity and telecommunications borrowers, we focused on the end of calendar year 1995, the most recent year for which RUS had information available on the programs' borrowers, and the preceding 3 calendar years.

To compile background information and to gain an understanding of how the utility loan programs operate, we interviewed numerous RUS officials, including the Assistant Administrators and/or Deputy Assistant Administrators for electricity, telecommunications, and water and waste disposal. We reviewed the basic statutory authority for the programs—the Rural Electrification Act of 1936, as amended, for the electricity and telecommunications programs and the Consolidated Farm and Rural Development Act, as amended, for the water and waste disposal programs—and relevant parts of RUS' implementing regulations and internal policy guidance. We also reviewed RUS' various publications, pamphlets, and reports that describe the utility loan programs and USDA's Budget Explanatory Notes for Committee on Appropriations for fiscal years 1994 through 1997. Furthermore, we reviewed prior reports by GAO and USDA's Office of Inspector General that were issued during fiscal years 1992 through 1996. Finally, we reviewed the provisions that apply to RUS and its utility loan programs that are contained in the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act of 1994.

To compile information on the number and dollar amount of loans that RUS made or guaranteed during fiscal years 1992 through 1996 and on RUS' subsidy and administrative costs for operating the utility loan programs during those years, we used RUS' various financial reports, the Department's budget explanatory notes, and information provided to us by the Budget Division in USDA's Rural Development mission area. During the

course of our study, we provided RUS with schedules of the loan and cost information that we had compiled; RUS officials reviewed these schedules and did not suggest any revisions to the tabulated data. The descriptive information on credit reform was extracted from prior GAO reports.

Most of the financial data presented in this report are unaudited information that we extracted from RUS' reports and automated records. We did not verify the accuracy of the information contained in the agency's reports and automated records.

Our analysis of the financial condition of RUS' portfolios covered fiscal years 1992 through 1996. To determine the financial condition of the electricity, telecommunications, and water and waste disposal loan portfolios, we reviewed RUS' financial reports, other information that RUS provided to us, and data contained in the agency's automated records. We used these data sources to compile information on outstanding principal in each program and the portion of outstanding principal that was owed by delinquent borrowers at the end of fiscal years 1992 through 1996, and the extent of restructuring and/or reamortizing of loans and the losses that RUS has incurred during these years. We did not adjust the outstanding loan amounts to reflect the allowance for losses that RUS includes in its financial statements nor did we assess the adequacy of reserves on the loans. During the course of our study, we provided RUS with schedules of the outstanding and delinquent loan information that we had compiled; RUS officials reviewed these schedules and did not suggest any revisions to the tabulated data.

Additionally, to identify problem borrowers other than those that were delinquent, we interviewed, among others, the Program Advisor in the Financial Services Staff—the RUS office that works on resolving problem loan accounts—the Director of the Electric and Telephone Financial Operations Division, and the Director of the Power Supply Division in the electricity program. We compiled specific information on each problem borrower from the agency officials we interviewed and from RUS' financial reports and automated records.

Our analysis of the financial characteristics of borrowers covered calendar years 1992 through 1995. To determine the financial characteristics of borrowers having electricity and telecommunications loans, we reviewed RUS' annual statistical reports covering calendar years 1992 through 1994 that contain financial information submitted by electricity and telecommunications borrowers. Although borrowers had submitted to RUS

financial information for calendar year 1995 and the agency had prepared the automated files that are used to produce the 1995 annual statistical reports, it had not published the reports until our work was close to being completed. In addition, we accessed the agency's automated files for calendar years 1992 through 1995 containing the borrower-submitted information that is used to prepare the annual statistical reports.

We used the annual statistical reports to identify the financial information to extract from the automated files. We used the automated files to analyze selected balance sheet and income statement information, including borrowers' current and total assets, current and total liabilities, net worth (equity), operating revenues, operating expenses, operating income, and net income (profit or loss). We analyzed similar information for all borrowers who submitted financial information to RUS.

For each calendar year, we calculated totals and averages for the selected balance sheet and income statement items. We also used the balance sheet and income statement information to calculate various financial ratios for each borrower, including current ratio, debt-to-asset ratio, and times-interest-earned ratio. We categorized borrowers in ranges of the various balance sheet and income statement items and in ranges of the ratios. This allowed us to use consistent information to analyze borrowers in these two programs. RUS uses some of these same items and measures in its monitoring of borrowers.

We did not verify the accuracy of the financial submissions from the borrowers to RUS. However, we did perform various tests to ensure the correctness of the information contained in the automated files, such as whether assets less liabilities equals net worth, operating revenues less operating expenses equals operating income, and operating income plus or minus nonoperating income/expenses and adjustments equals net income (profit or loss). When the balance sheet or income statement information did not equal, we excluded the borrowers from the analyses for the year(s) in question. Specifically, we excluded five electricity distribution borrowers for calendar year 1994, one telecommunications borrower for 1995, three telecommunications borrowers for 1994, and four telecommunications borrowers for 1993. We verified that the correct information had been extracted from the automated records by, for example, comparing those data with information in RUS' 1992 through 1995 statistical reports for electricity and telecommunications borrowers. We also compared the results of our computation of the times-interest-earned

ratios with those contained in the 1992 through 1995 reports for electricity distribution and telecommunications borrowers.

The results of our analysis covered more borrowers than are covered in RUS' annual statistical reports because, for example, we included borrowers that submitted information to RUS after the submission date for publishing its annual reports. The information submitted after that date is maintained in the agency's automated files. Also, while our analysis covers most borrowers with electricity and telecommunications loans, some borrowers are excluded because they did not submit financial information to RUS. For example, the automated files covering 1995 did not have financial information on 74 borrowers.

We did not attempt to determine the financial characteristics of the borrowers with water and waste disposal loans because most are public entities rather than private firms.

We conducted our review from April 1996 through February 1997 in accordance with generally accepted government auditing standards. USDA reviewed a draft of this report. The Department's comments are contained in appendix IV.

Major Contributors to This Report

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